

(H. B. 3)

(No. 9-2017)

(Approved February 8, 2017)

AN ACT

To amend Sections 2, 11, 19, 44, 51, and 61, add a new Chapter IV, renumber current Chapter IV and Sections 69, 70, 71, and 72 of Act No. 219-2012, as amended, known as the “Trust Act”; amend Sections 1032.08, 1033.09(a)(3), 1033.09(a)(1)(A)(ii)(I), 1081.01(a)(11)(B), 1081(a)(11)(B), 1081.01(d)(3), 1081(e)(2)(B), 2022.01(b), 2023.02(b)(2), and 1033.09(a)(1)(C) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” in order to incorporate incentives to retain and enable the return of professionals to Puerto Rico; incentivize the creation of retirement plans; make technical amendments; and for other related purposes.

STATEMENT OF MOTIVES

Professionals are leaving Puerto Rico at an accelerated and concerning rate. Since 2004, the continuous financial crisis faced by our Island and the lack of employment opportunities have forced our people to abandon our coasts in search for better opportunities to guarantee their future and that of their families. We are fully aware and proud to have world-class human resources in Puerto Rico. Likewise, employers outside of Puerto Rico have discovered, within our Island, a wealth of talent available for export.

However, it is also a reality that due to the lack of capability to implement cost reduction policies, the preceding administration resorted to imposing a large number of new taxes. These taxes further increased the burden on the working class, given that they raised the cost of living and of working in Puerto Rico, and as a result: our Island is being vacated at an accelerated rate and the economic indicators are in a downward spiral. In view of the foregoing, our human resources have been

forced to move elsewhere, mainly to one of the 50 states of our Nation, thus depriving our society of the same human resources that can lead us out the crisis we are facing.

From the total number of Puerto Ricans that have left the Island, 159,794 left between 2004 and 2012 for an average of 19,974 persons per year. However, since 2012, the People's despair and lack of trust in the government have increased these numbers substantially. From 2012 to July 1, 2015, the number of residents that left our Island increased to an average of 55,114 persons per year.

This government plans to do everything within its power to protect and retain our human resources as well as attract productive talent. In order to achieve this, it is indispensable to safeguard their personal growth and future stability.

In the interest of stopping the massive exodus of the Puerto Rican professional class and safeguarding its future and that of their families, this Act amends the "Trust Act" and the Internal Revenue Code to provide a better and broader protection of assets to incorporate the concept of the Retirement Plan Trust, address statutory conflicts, protect surviving spouses, and create opportunities to enable private employers to offer retirement plans. The foregoing is consistent with our Plan for Puerto Rico by making our Island a better place for investments and coexistence.

In order to understand these amendments, we must keep in mind that the assets subject to a trust are protected given that they stem from the estate of the trustor. Since the trustor disengages from its administration, the assets are considered a separate estate, and as such, shall have full juridical personality (not attenuated). Therefore, under this Act, and in order to provide greater certainty and security guarantees to the administered estate, the trust may contract and record the assets in its name thus simplifying administrative measures and reducing any uncertainties that may occur when there is a change in trustee. Moreover, this Act facilitates the trust's administration and reduces the number of times it resorts to a judicial forum.

For example, it provides a swift and simple procedure to fill the vacancies of trustees without judicial intervention. With respect to the trust assets, it provides broader protections for accrued income in order to be exclusively attached or executed to satisfy the pensions of spouses, former spouses, or children.

In contrast to these protections, the circumstances in which the trust may be dissolved are established. Previously, a trust could be terminated through the express and personal consent of the parties that constituted said trust, by an agreement between the beneficiaries, or by a decision of the trustors. This amendment requires the unanimous and express consent of all trustors and beneficiaries if the trustor is alive. Lastly, a new Chapter IV is added to the “Trust Act” in order to incorporate the Retirement Plan Trust, which, although recognized in the Internal Revenue Code, did not appear in the provisions of the “Trust Act.” Furthermore, as part of this new Chapter IV, federal guidelines are incorporated, and it is further provided that in the event of the death of the participant in the Retirement Plan, the beneficiary, in first instance, shall be the surviving spouse without being subject to the estate division process. Therefore, the continuity of the family income is guaranteed, thus preventing the spouse from becoming a burden for society after widowhood.

Regarding the Internal Revenue Code, the amendments are directed toward increasing to \$75,000 the cap on deductions allowed for contributions to retirement plans. Furthermore, the amendments introduced under this Act render the requirements for retirement plans that benefit professionals denominated as owner-employees flexible and also incentivize more small- and medium-sized businesses (PYMES) to create retirement plans for their employees. Similar to the amendments of the “Trust Act,” it also provides that in the event of the death of a participant in a Retirement Plan, the beneficiary shall be the surviving spouse without resorting to an estate division process.

All these amendments converge for the purpose of making retirement plans more flexible and broad, making the establishment thereof less onerous, even for small businesses, and thus incentivizing the creation of retirement plans as well as guaranteeing the future livelihood of professionals and their families. Furthermore, the process that begins upon the death of a participant is also simplified, so that it does not become an obstacle for a family's livelihood. In this manner, we do justice to our professionals who, after many years of education, spend their lives saving in order to have a decent retirement and the peace of mind that, upon their death, their families will be in a position to subsist.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF PUERTO RICO:

Section 1.- Section 2 of Act No. 219-2012, as amended, known as the "Trust Act," is hereby amended to read as follows:

"Section 2.- Autonomous Estate.

Trust property or rights constitute a fully autonomous estate separate from the personal estate of the trustor, trustee, and beneficiary that is limited to a specific purpose as determined at the time of the constitution thereof.

Once the deed of trust has been executed and recorded, pursuant to the provisions of this Act, a juridical entity independent of its trustors, trustees, and beneficiaries shall be constituted, enjoying full juridical personality.

..."

Section 2.- Section 11 of Act No. 219-2012, as amended, known as the "Trust Act," is hereby amended to read as follows:

"Section 11.- Trust Property.

The trust is the owner of all property in trust, whether real or personal. Real property held in a trust shall be recorded in the Property Registry under the name of the trust."

Section 3.- Section 19 of Act No. 219-2012, as amended, known as the “Trust Act,” is hereby amended to read as follows:

“Section 19.- Successor Trustees.

...

If the trust instrument fails to set forth the manner in which a vacancy shall be filled, the successor trustee shall be selected by the unanimous agreement of the beneficiaries. If the beneficiaries fail to reach an agreement, the successor trustee shall be designated by the court.

...”

Section 4.- Section 44 of Act No. 219-2012, as amended, known as the “Trust Act,” is hereby amended to read as follows:

“Section 44.- Rights of Creditors.

Creditors shall have the following rights with regards to the trust’s assets, principal, or capital:

(a) Except as expressly provided in subsection (b) of this Section, a creditor of the beneficiary of a trust shall have over or with regards to such beneficiary’s interest or the property under said trust those rights that have been expressly granted thereto by the terms of the instrument that creates or defines the trust or by the laws of Puerto Rico or any applicable federal law.

...

(b) Any interest in a trust, in trust property, or in the revenues or income generated by the trust assets that are not subject to the rights of a beneficiary’s creditors pursuant to this Section shall be exempt from foreclosure, attachment, eviction, auction, and any other remedy or legal proceedings filed by or on behalf of any creditor, including, but not limited to, legal actions or claims against one or more trustees or other beneficiaries seeking a remedy that directly or indirectly affect the

beneficiary's interest, such as, for example, but not limited to, an order issued at the request of a creditor or the court itself that could:

(i) ...”

Section 5.- Section 51 of Act No. 219-2012, as amended, known as the “Trust Act,” is hereby amended to read as follows:

“Section 51.- Ineffectiveness of Spendthrift Provision with Respect to the Beneficiary of Income.

Notwithstanding a spendthrift provision included in a trust as provided in subsection (g) of the preceding Section, an income beneficiary's creditor or assignee may reach the beneficiary's income interest by means of attachment or execution when the creditor's claim to his assignee is to satisfy the support obligation provided in the Civil Code; and in any other case required under federal law.”

Section 6.- Subsection (f) is hereby amended, a new subsection (g) is hereby added, the subsequent subsections are hereby renumbered, and the current subsection (k) is hereby eliminated of Section 61 of Act No. 219-2012, as amended, known as the “Trust Act,” to read as follows:

“Section 61.- Termination of Trust.

A trust shall terminate when:

(a) ...

...

(f) during the lifetime of the trustor, by unanimous and express consent of all the trustors and beneficiaries, provided that said power has been set forth in the trust deed;

(g) after the death or incapacitation of the trustor or all of the trustors by a court, all the beneficiaries agree thereto if they are determined and capable, unless continuation of the trust is necessary to fulfill an essential purpose thereof. However, if any of the beneficiaries is not determined or is unfit, or if any of them does not

consent to the early termination of the trust, the remaining beneficiaries may partially terminate the trust, provided, that it is not detrimental to the remaining beneficiaries;

(h) the beneficiary resigns, becomes incapacitated, is removed or rejected, or dies, provided that the clear intention of the trustor was that only such person could be the trustee;

(i) the object upon which it was constituted is destroyed. However, if the destruction of the object of the trust is the fault of the trustee or a third party, the trust shall not terminate and its estate shall be cause of action against the trustee for breach of trust or against the third party under tort liability;

(j) a resolution of the right of the trustor over the trust assets; or

(k) there is a confusion between the nature of sole beneficiary and that of sole trustee.

...”

Section 7.- A new Chapter IV is hereby added to Act No. 219-2012, as amended, known as the “Trust Act,” to read as follows:

“CHAPTER IV
RETIREMENT PLAN TRUSTS

Section 69.- Definitions.

(a) Retirement Plan Trust is defined as a trust qualified under Section 1081.01(a) et seq. of the Internal Revenue Code for a New Puerto Rico, Act No. 1-2011, as amended;

(b) Trustor shall have the same definition provided therefor in Section 13 of this Act;

(c) Owner-employee shall have the same definition provided therefor in the Internal Revenue Code for a New Puerto Rico, Act No. 1-2011, as amended;

(d) Self-employed Individual shall have the same definition provided therefor in the Internal Revenue Code for a New Puerto Rico, Act No. 1-2011, as amended;

(e) Participant shall be defined as a person who is entitled to receive lifetime payments from the Retirement Plan Trust.

(f) For purposes of this Chapter IV, beneficiary shall be defined as the person designated to receive the full amount of the retirement plan account upon the death of the participant.

Section 70.- Designation of Beneficiary.

If the participant is married, the spouse shall be the beneficiary who shall be exclusively entitled to the total benefits payable under the plan in the event of the participant's death. Notwithstanding the foregoing, the participant may designate a beneficiary other than the spouse, provided such designation complies with the provisions of Section 205(c)(2) of the Employee Retirement Income Security Act of 1974, as amended, or any other federal statute that substitutes it.

No spouse consent shall be necessary to designate another beneficiary if the retirement plan trust is exempt from the Employee Retirement Income Security Act of 1974, and the participant and his spouse have signed a prenuptial agreement establishing the community property regime.

Section 71.- Estate Tax Exemption.

All assets of a Retirement Plan Trust shall be excluded or exempt from the provisions on Successions and Inheritance of the Puerto Rico Civil Code and the disposition thereof shall be determined in accordance with the terms of the document or documents that govern the Retirement Plan Trust.”

Section 8.- Current Chapter IV, and Sections 69, 70, 71, and 72 of Act No. 219-2012, as amended, known as the “Trust Act,” are hereby renumbered as Chapter V, and Sections 72, 73, 74, and 75, respectively.

Section 9.- Section 1032.08(h) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 1032.08.- Amounts Received Under Accident or Health Plans.–

(a) ...

...

(h) Self-employed Individuals shall be considered employees.- For the purposes of this Section, the term ‘employee’ includes an individual who is self-employed or who works independently.”

Section 10.- Section 1033.09(a)(3) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 1033.09.- Contributions by an Employer to Employees’ Trust or Annuity Plan and Compensation Under a Deferred-payment Plan.–

(a) ...

(1) ...

(2) ...

(3) Self-employed Individuals.- In the case of a plan included in paragraph (1) which provides contributions or benefits for employees some or all of whom are owner-employees as said term is defined in Section 1081.01(e)(3), and at the same time is an employer as said term is defined in Section 1081.01(e)(4) –

(A) the term ‘employee’ also includes an individual who is an owner-employee;

(B) the term ‘earned income’ has the meaning established in Section 1081(e)(2);

(C) the contributions to such plan on behalf of an individual who is an owner-employee shall be considered to satisfy the conditions of ordinary and necessary expenses of clause (a) of this Section, up to the limit to which the contribution made for the individual's benefit does not exceed the annual limit provided in Section 1081.01(a)(11)(B) of the Code, or twenty-five percent (25%) of the income earned by said individual (determined without considering the deductions allowable under this subparagraph) derived from the trade or business with respect to which said plan is established, and to the extent that said contributions are not attributable (determined in accordance with the regulations prescribed by the Secretary) to the purchase of life, accident, health, or other insurance; and

(D) ...
...”

Section 11.- Section 1033.09(a)(1)(A)(ii)(I) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 1033.09.- Contributions by an Employer to Employees’ Trust or Annuity Plan and Compensation Under a Deferred-payment Plan.

(a) ...

(1) ...

(A) ...

(i) ...

(ii) In the case of defined contribution pension plans.—

(I) In the taxable year when paid, if the contributions are paid into a defined contribution pension plan trust, and if such taxable year ends within or with a taxable year of the trust with respect to which the trust is exempt under Section 1081.01(a), in an amount not in excess of twenty-five percent (25%) of the compensation otherwise paid or accrued during the taxable year

to all employees under the defined contribution pension plan. Notwithstanding the foregoing, those contributions made to a defined contribution pension plan that do not exceed the annual limit provided in Section 1081.01(a)(11)(B) of the Code, not including contributions transferred from another qualified retirement plan, shall be considered as deductible under this Section. If in any taxable year beginning after December 31, 1953, there are paid into the trust, or a similar trust then in effect, amounts less than the amounts deductible under the preceding sentence, the excess, or if no amount is paid the amounts deductible, shall be carried over and deductible, when paid in the succeeding taxable years in order of time, but the amount so deductible under this sentence in any such succeeding taxable year shall not exceed twenty-five percent (25%) of the compensation otherwise paid or accrued during such succeeding taxable year to the beneficiaries under the plan. In addition, any amount paid into the trust in a taxable year beginning after December 31, 1953, in excess of the amount allowable with respect to such year under the preceding provisions of this item shall be deductible in the succeeding taxable years in order of time, but the amount so deductible under this sentence in any one such succeeding taxable years together with the amount allowable under the first sentence of this item shall not exceed twenty-five percent (25%) of the compensation otherwise paid or accrued during such taxable year to the beneficiaries under the plan. If the contributions are made to two or more defined contribution plan trusts, such trusts shall be considered a single trust for purposes of applying the limitations in this item. ...”

Section 12.- Section 1033.09 (a)(1)(C) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to add a sentence to read as follows:

“Section 1033.09.- Contributions by an Employer to Employees’ Trust or Annuity Plan and Compensation under a Deferred-payment Plan.

(a) ...

(1) ...

(A) ...

(B) ...

(C) ... Notwithstanding the foregoing, those contributions that do not exceed the annual limit provided in Section 1081.01(a)(11)(B) of the Code, not including contributions transferred from another qualified retirement plan shall be considered as deductible under this Section.”

Section 13.— Section 1081.01(a)(11)(B) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 1081.01.— Employee Trusts.—

(a) ...

(1) ...

...

(10) ...

(11) ...

(A) ...

(B) In the case of a defined contribution plan, the annual contributions by the employer and the participant, and other additions with respect to a participant, without including contributions rolled over from another qualified retirement plan, shall not exceed the lesser of:

(i) seventy-five thousand dollars (\$75,000).

(ii) twenty-five percent (25%) of the Net Income.

(C) ...

...”

Section 14.– Section 1081.01(d)(3) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 1081.01.- Employee Trusts.

...

(d) ...

(1) ...

(2) ...

(3) ...

(A) ...

(i) ...

(ii) ...

(I) ...

(II) The excess of the actual deferral percentage

for the group of highly compensated employees over that of all other eligible employees shall not exceed two (2) percentage points and the actual deferral percentage for the group of highly compensated employees shall not exceed the actual deferral percentage of all other eligible employees multiplied by two (2).

If two (2) or more plans which include cash or deferred contribution arrangements are considered as one plan for purposes of subsections (a)(3) and (4), the cash or deferred contribution arrangements included in such plans shall be treated as one arrangement for purposes of this item.

If any highly compensated employee is a participant under two (2) or more cash or deferred employer contribution arrangements, all cash or deferred contribution arrangements shall be considered a single arrangement for purposes of determining the deferral percentage with respect to said employee.

Notwithstanding the foregoing, the determination rules of this subsection (d)(3) shall not apply to retirement plans with less than one hundred (100) participants whose business generate less than ten (10) million dollars annually in gross income, subject to the employers providing a benefit to all eligible employees of not less than three percent (3%) of their compensation.

(B) ...

(C) ...

(D) ...

(E) ...

(i) ...

(ii) ...

(iii) **Highly Compensated Employees.**— For purposes of this clause, the term ‘highly compensated employees’ means any employee who:

(I) owns five percent (5%) or more of the voting stock or the total value of all the classes of stocks of the corporation that is a participating employer;

(II) owns five percent (5%) or more of the capital or profit interest of the employer, in the case of an entity that is not a corporation; or

(III) for the preceding taxable year had a compensation from the employer in excess of one hundred fifty thousand dollars (\$150,000);

(IV) in order to determine whether an employee owns five percent (5%) or more of the stock, capital, or profits, there shall be taken into account the rules of the controlled group of the employer, as defined in Section 1010.04, of the group of related entities, as defined in Section 1010.05, and of the affiliated service group, as defined in Section 1081.01(a)(14)(B).”

(4) ...

Section 15.- Section 1081.01(e)(2)(B) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 1081.01.- Employee Trusts.

...

(e) Definitions and Rules Related to Self-employed Individuals and Owner-employees. — For purposes of this Section —

(1) ...

(2) ...

(A) ...

(B) For the purposes of this subsection, the term ‘earned income’ includes gains, other than any gains under any other provision of this Subtitle treated as gains from the sale or exchange of a capital asset, and net gains derived from the sale or other disposition of, or the authorization of the use of property (other than good will) by an individual whose personal efforts created such property.”

Section 16.- Section 2022.01(b) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 2022.01.- Definition of Decedent’s Gross Estate.

(a) ...

(b) Property Transferred with Reserved Rights in Favor of the Transferor.— The decedent’s gross estate includes, up to the amount of the share in such estate that is attributable to the decedent, the value of any property transferred by the decedent while living if:

(1) He retained possession and use of the property or any part thereof, or if he received or was entitled to receive a life annuity or the income from the transferred property; or

(2) He retained the right, either alone or in conjunction with another person, to designate the persons who shall possess or enjoy the property, the life annuity, or the income therefrom.

(3) Notwithstanding the foregoing, in those cases where the property was transferred to a trust in Puerto Rico whose trustee is not the decedent, and the decedent was a resident of Puerto Rico at the time of his death, said property shall not be included in the decedent's gross estate even if the decedent is the beneficiary of said trust, if the trust does not terminate by reason of the death of the decedent, and no collation of trust assets shall be required to comply with the provisions of the Civil Code.

(c) ...
...”

Section 17.- Section 2023.02(b)(2) of Act No. 1-2011, as amended, known as the “Internal Revenue Code for a New Puerto Rico,” is hereby amended to read as follows:

“Section 2023.02

(a) ...

(b) ...

(1) ...

(2) Stock issued by any domestic corporation or partnership.

(3) ...”

Section 18.- Severability.

If any clause, paragraph, subparagraph, sentence, word, letter, article, provision, section, subsection, title, chapter, subchapter, heading, or part of this Act were held to be null or unconstitutional, the ruling, holding, or judgment to such effect shall not affect, impair, or invalidate the remainder of this Act. The effect of said holding shall be limited to the clause, paragraph, subparagraph, sentence, word, letter, article, provision, section, subsection, title, chapter, subchapter, heading, or part of this Act thus held to be null or unconstitutional. If the application to a person or a circumstance of any clause, paragraph, subparagraph, sentence, word, letter, article, provision, section, subsection, title, chapter, subchapter, heading, or part of this Act were held to be null or unconstitutional, the ruling, holding, or judgment to such effect shall not affect or invalidate the application of the remainder of this Act to such persons or circumstances where it may be validly applied. It is the express and unequivocal will of this Legislative Assembly that the courts enforce the provisions and application thereof to the greatest extent possible, even if it renders ineffective, nullifies, invalidates, impairs, or holds to be unconstitutional any part thereof, or even if it renders ineffective, invalidates, or holds to be unconstitutional the application thereof to any person or circumstance. This Legislative Assembly would have approved this Act regardless of any determination of severability that the Court may make.

Section 18.- Effectiveness.

This Act shall take effect immediately after its approval.